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Supreme Court of the United States

October Term, 1948

No. 628

Commerce Company, *Petitioner*,

v.

United States of America, *Respondent*

On Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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BRIEF OF AMICUS CURIAE

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Wilson - Epes Printing Co. - RE 6003 - Washington 1, D. C.

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MOTION FOR LEAVE TO FILE BRIEF OF AMICUS CURIAE

The Undersigned Respectfully Moves This Honorable Court for Leave to File the Annexed Brief as *Amicus Curiae*.

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BRIEF OF AMICUS CURIAE

The case of *Virginian Hotel Corporation v. Helvering,* 319 U. S. 523, No. 766, October Term 1942, decided by a vote of five to four, appears to me to govern this case. But the clear absurdity of the *Virginian Hotel* decision, as demonstrated by the result of applying it to the present case, strongly demands that certiorari be granted in this case so that the applicable rules of law may be re-examined.

It is safe to say that there is no reasonable likelihood that this Court would have decided as it did in the *Virginian Hotel* case had the facts of the present case been before it.

The *Virginian Hotel* case involved a situation where depreciation on property at certain rates had been shown on tax returns in a series of profit years, and then throughout in a series of subsequent loss years, and then in a series of later profit years. The Commissioner corrected the rate of depreciation in the second series of profit years on the ground that the correct depreciation rate was less than that claimed. The property had a longer life than had been claimed. When the rate was corrected in the later profit years, the taxpayer urged that it should be permitted to correct the excess depreciation in the loss years, for purposes of determining the correct basis of the property at the beginning of the second series of profit years. The Court held that the taxpayer was not entitled to correct the rate in the *preceding* loss years, although no tax loss resulted to the government from the excess depreciation claimed in those years. There was confusion in the argument and brief for the Commissioner as to whether there was a real error in the earlier years or whether the estimate of useful life was reasonable when made and simply turned out in later years to have been a mistake in judgment.[1] And that confusion colored the whole case.

[1] This confusion is apparent from a reading of the Government's brief on the merits in the *Virginian Hotel* case, which reveal clearly that the Government was objecting to a taxpayer being able retroactively to change depreciation allowances claimed when, *because of future events*, the original estimate turned out to be wrong. The Solicitor General's argument in that case was not directed squarely to a situation where a clear error was made at the time of filing of the return and where the Commissioner would have disallowed part of the amount claimed if he had investigated the return the day it was filed. Extracts from the Government's brief on the merits in the *Virginian Hotel* case which illustrate the

The present case presents the issue involved in the *Virginian Hotel* case in such a way as to leave no trace of doubt that what is involved is a true error on the part of the taxpayer, not just a bad choice by the taxpayer between two permissible claims. In fact, the government's treatment of the taxpayer in the present case shows conclusively that the government recognizes the error in the depreciation claimed to have been a genuine error. *And the error was determinable, and has actually been determined, even for years prior to the loss years for which correction has been refused.*

In the present case the buildings involved were constructed in 1929. Profits were made in 1929, 1930 and 1931. There were losses in 1932, 1933, 1934 and 1935. The same depreciation was shown in the returns for all years. In a conference in 1936 covering the years 1929 to 1931, it was agreed between the taxpayer and the Commissioner that the rate was excessive, and the taxes due by the taxpayer for 1929, 1930 and 1931 were increased because of the correction of the error in the depreciation claimed. Nevertheless the Commissioner has refused to correct the error in the loss years, 1932 to 1935.

In other words, the Commissioner has insisted that the basis of the property reflect the erroneous depreciation shown on the returns during those loss years, even though the Commissioner has already collected additional taxes by correcting the error in the *preceding* profit years. It is clear that at the time the tax returns showing the excessive depreciation were filed, the depreciation was erroneous to the extent of the excess. The result is so obviously absurd

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confusion in the Government's presentation of the case to this Court are printed as an appendix to this brief.

If any examination is made of the briefs in the *Virginian Hotel* case, it is suggested that the briefs on rehearing bound with the briefs and records of the October Term 1943 be examined.

as to refute any construction of an ambiguous statute which requires such result.

If this Court had had such facts before it in the *Virginian Hotel* case, it seems hardly conceivable that any member of this Court would have concluded that, in computing the basis of its property at January, 1938, the taxpayer had to deduct the erroneous amounts shown on the returns for 1932 to 1935, even though the Government had suffered no harm from the showing of these erroneous amounts on the return, and even though the Commissioner had already admitted the error by correcting the deduction for 1929 to 1931 and for the years following 1935. No reason can be suggested why Congress would even consider passing a law which would require such a result. If the *Virginian Hotel* decision requires such a result — and its language does seem to require it — the decision should be reexamined without delay.

If the *Virginian Hotel* decision does apply to the present case it is obvious that the effect of the decision is to bind a taxpayer in computing his taxes in subsequent years by an error made in preceding years, where the government has not suffered and the taxpayer has not benefited in any way by the error. Never in the whole history of income taxes has Congress or have the Courts evidenced the slightest inclination to bind a taxpayer by errors made in preceding years, except where some injury has resulted to the Government upon which estoppel might be based. It is a fundamental principle of our income tax system that each year stands on its own basis and that the tax for each year is to be *correctly determined.* If there is to be a departure from this universal principle in some particular case, based on errors in returns for other years, this Court should demand the clearest showing that Congress has required it.

The legislative history of Section 113(b)(1)(B) makes it clear that Congress never even considered the possibility

of such a result, but rather was merely seeking, in enacting Section 113(b)(1)(B), to make it clear that where a taxpayer had reduced his taxable income by excessive depreciation—depreciation in excess of "allowable" depreciation—he could not restore that amount to his basis and in effect get to deduct it again. The statute was not aimed at penalizing errors shown on returns. It was aimed at preventing the double *use* of deductions in computing taxes—not at the meaningless writing of figures on returns where no taxes were due even in the absence of those figures. Congress was clearly enacting a statutory estoppel and nothing more. And there is nothing in the statute or in its legislative history to suggest that the estoppel should apply where injury, a necessary element of all estoppel, was absent.

It is impossible in the short space of an amicus brief on petition for certiorari to argue the matters which should be argued in the presentation of this case to the Court. But it is respectfully requested that at a time when unanimous decisions of the Supreme Court of many years standing are being reexamined and reversed, the decision in the *Virginian Hotel Corporation* case should not be permitted to stand in the light of the obviously absurd results which it requires.

Respectfully submitted,

W. A. SUTHERLAND,
Amicus Curiae

APPENDIX

Extracts from Brief for the Commissioner in the Virginian Hotel Case

* * * *

The taxpayer, however, would turn the rate reduction to its definite advantage. Except insofar as the statutes have specifically provided for loss carry-overs, the revenue laws do not contemplate that a taxpayer shall be allowed to take advantage in a later year of deductions available in earlier years which gave it no tax benefit because of insufficiency of income. Each tax year stands on its own footing. Burnet v. Sanford & Brooks Co., 282 U. S. 359. Consistently with the depreciation schedule which had been employed since 1927, with the approval of the Commissioner, the taxpayer continued to take these deductions through its loss years 1931-1936. *The deductions were actually available to it, just like any other deduction to which it was then entitled, although it was subsequently found that the amount had been excessive.* Indeed, the taxpayer continued to use the same rate in the year 1937 when it had net income and admittedly derived a tax benefit from the excessive claim, which it could not have done if it had undertaken to reduce the rate. Ordinarily the taxpayer could not expect to recoup the deductions wasted in its bad years. What its position here means is that the necessity of having to reduce the rate in 1938 should serve as an occasion to permit it to recoup its wasted deductions. This would not have been permitted if the rates had not been changed; there is no reason why this circumstance should serve as an excuse. (p. 13)

* * * *

The statutory allowances for depreciation provide a taxpayer an opportunity to recover tax-free his investment in property which is used in producing income and is being consumed or is deteriorating in the process. In taking the deductions, he is required to estimate in advance the anticipated life of the property and is required to spread the deductions over that estimated life. Thus, if he estimates that the property will have a useful life of 20 years, he will each year

deduct from income 1/20 of the cost or other basis of the property; accordingly, over the 20 years he is deriving income from the property he will be permitted to take deductions equal to his investment in the property.

Based as it is on beforehand estimates of useful life, the method, of course, cannot be precise and adjustments will sometimes be necessary. *Experience with the property will often show that the useful life of the property has been overestimated or underestimated. When this occurs, a new estimate is made, and the basis of the property, to the extent that it has not been recovered by prior deductions, is spread over the remaining life as thus reappraised.*[2] This is accomplished under the statute involved here, by reducing the original basis by depreciation previously "allowed," or that "allowable," whichever amount is greater, and by applying to this adjusted basis the new rate calculated upon the new estimate of useful life. For example, if after 15 years it were determined that property, instead of having a 20-year life (with 5 years remaining), had a 25-year life (with 10 years remaining), the remaining unrecovered basis would be spread over 10 years instead of 5. As a consequence, the deduction for each year would be half as large as under the original computation, but the privilege of taking depreciation deductions would last twice as long. (pp. 9-11)

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[all italics added]

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[2] No adjustment is made for the depreciation deductions *for the years preceding the reappraisal* which are still open under the statute of limitations. Sample-Durick Co. v. Commissioner, 35 B. T. A. 1186.